EXHIBIT OO

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

In re:
THE FINANCIAL OVERSIGHT AND
MANAGEMENT BOARD FOR PUERTO RICO,
as representative of
THE COMMONWEALTH OF PUERTO RICO, et al.
Debtor,
--X
In re:
THE FINANCIAL OVERSIGHT AND
MANAGEMENT BOARD FOR PUERTO RICO
as representative of
THE EMPLOYEES RETIREMENT SYSTEM OF
THE GOVERNMENT OF THE
COMMONWEALTH OF PUERTO RICO,
Debtor.

450 Park Avenue
New York, New York
June 20, 2019
2:03 P.M.

EXAMINATION BEFORE TRIAL of LAWRENCE SHER, an Expert Witness herein, taken by the attorneys for the respective parties, pursuant to Notice, held at the above-stated time and place, before Melissa Leonetti, RPR, a Notary Public of the State of New York.

L. SHER

THE VIDEOGRAPHER: We are now on the record. This is the video deposition of Lawrence Sher in the matter of In Re: Financial Oversight and Management Board for Puerto Rico, et al., held at the offices of Jones Day, 450 Park Avenue, New York, New York, on Thursday, June 20th, at approximately 2:03 p.m.

I am Chris Ritona, the videographer with Advanced Depositions. The court reporter today is Missy Leonetti, also with Advanced Depositions. We are from the office in Philadelphia, PA.

All counsel will be noted on the stenographic record. The court reporter will now please swear in the witness.

LAWRENCE J. SHER, after having first been duly sworn by a Notary Public of the State of New York, was examined and testified as follows:

EXAMINATION BY
DAVID R. FOX, ESQ.:

Q. Dr. Sher, can you please state your name for the record.

A. Lawrence J. Sher.

L. SHER

Pay as You Go, but I understand them to be the same.

Q. How do you understand the term? I'm sorry.

A. The Pay-Go term is very specific to this case. I don't think I've heard it quite expressed like that before. I understand it's quite analogous to what you would say a Pay-Go type of arrangement.

Q. Today would you understand if I use the term Pay-Go to refer specifically to Puerto Rico's Pay as You Go system and Pay as You Go to refer to as a Pay as You Go system in general? Does that make sense?

A. That's okay.

Q. Have you heard the term Pay-Go fee?

A. Yes.

Q. What do you understand that term to refer to?

A. Again, in the context of this case, it is a fee, an amount of money that's assessed to various employers who previously were participating employers in ERS to -- to help finance the current benefit payments to former participants in ERS.

Q. Do you know who the Pay-Go fee is paid to?

L. SHER

A. My understanding is that's it's paid to the Commonwealth.

Q. You used the word "contributions" in your report. Does that have a specific meaning to you as an actuary or does it depend on the context?

A. Well, I think it could depend upon the context. I can tell you generally how I view that.

MS. DALE: Wait for a question.

Q. Same question about the word "funding." You used the term "funding" a few times in your report. Is that a term that has a specialized meaning to you as an actuary or is that also --

A. As a general term, yes.

Q. What is that meaning?

A. Funding, to me, means from the standpoint of work I'm familiar with, which is pension actuarial work.

When you fund something, you have a trust fund that's set aside, segregated from other assets typically of the employer, that is receiving contributions from the employer and sometimes from employees and is earmarked to provide certain benefits to the plan's participants over time.

pension plans involved in New Jersey. They were sponsored either by the state or by some of the municipalities.

By the way, that also encompasses the study of healthcare benefits for retirees. And the purpose of the study was to try to come up with alternative ways of funding or providing benefits under the program to make it, you know, more sound from a financial perspective.

Q. What role did pension obligation bonds play in that work?

A. Well, it had -- it came up because they had entered into them, and there were some discussions about the possibility as you were going along of introducing them again.

Q. What was the nature of those discussions?

A. I think it was just together with a whole bunch of other possibilities. It wasn't as if it was -- it wasn't singled out as a likely prospect. It was just on the list of things that we were considering.

Q. Was any consideration given as part of your work in New Jersey to a transition to a Pay as You Go system?

A. I would say no, although there was a concern that some of the funds would run out of money. That's one of the things that triggered the study.

Q. Why did you mention the concern that some of the funds would have run out of money in response to my question about a transition to a Pay as You Go system?

A. Because what would happen is if it ran out of money, it might very well -- one possibility would be that it would have to transition over to a Pay as You Go system. That's one possibility.

Q. Why is that? Can you explain that.

A. Well, because if the fund -- if the fund is run dry and there's no more money, either someone has to come up with money to continue to fund the plan or they would -- something else would have to give. One of the other possibilities would be the pension payments would be ceased.

Q. You mentioned two possibilities. One is someone coming up with money to fund the plan; is that right?

A. Right. We talked about increasing taxes, reducing services in some areas, increasing

assessments to the -- you know, to the various employers.

There was real concern, though, that if it ran out of money that whatever they were to do they ought to do it sooner rather than later, because they didn't really want to have to deal with some of the extreme possibilities.

Q. If the fund did run out of money and it wanted to continue to pay pension benefits as they were owed, is there an alternative to a transition to a Pay as You Go system under those circumstances?

MS. DALE: Objection. Are we talking about his work in New Jersey or just hypothetically or --

MR. FOX: Hypothetically.

A. I would say yes, it's pension payments and --

Q. Other than that?

A. Pension benefits are reduced, and they, again, try to find some other kind of funding. Free up money from -- one of the things they considered was freeing up money from healthcare, because the healthcare benefits were considered to be very rich.

They would have to find money elsewhere

L. SHER

in the budget or raise taxes, which they could do at that point. I mean, they -- they were talking about raising taxes in various ways.

Q. Going back for a moment to Appendix 3 in Exhibit 1. You have a list of publications in this document?

A. Yes.

Q. Were any of these published in an academic periodical?

MS. DALE: Objection to the form.

A. I would say -- you want me to go through them one by one? That's what I'm going to have to do to answer your question.

Q. If you don't know, you can say you don't know.

A. As I sit here now, I -- I know there are some. The answer is some.

Q. Okay. Do you know if any of them relate to a Pay as You Go pension system?

A. I don't think so.

Q. Are you an economist?

A. No.

Q. Are you qualified to render an economic opinion?

L. SHER

A. I would say no.

Q. And you're not a lawyer, right?

A. No.

Q. So you're not qualified to offer a legal opinion?

A. That's correct.

Q. Have you ever drafted pension reform legislation?

A. I would say yes.

Q. And is what you're thinking of your work in New Jersey?

A. No. I didn't draft any legislative language in that case, so no.

Q. What are you thinking of when you say you've drafted pension reform legislation?

A. That's something pretty recently where I was asked by an attorney to draft some language for a particular -- to amend a particular section of ERISA and the internal revenue code that would be consistent with changes that some of us want to see happen.

So I was asked by this person who was then in turn going to show it to congressional staff.

L. SHER

Q. Is this a change to legislation that governs private sector pensions?

A. That would be, yes.

Q. Are you an expert on the Uniform Commercial Code?

A. I would say no.

Q. Is that something you consider as an actuary?

A. Generally not.

Q. Is it something you considered in your report in this case?

A. No.

Q. Have you heard of section 9315 of the Uniform Commercial Code?

A. No.

Q. Are you an expert on the legal documents that govern bonds?

A. No.

Q. Did you consider any of the legal documents that govern the bonds at issue in this case?

A. No.

Q. So you have no opinion on whether anything in this case is Pledged Property under

those documents?

A. No.

Q. Employers Contributions?

MS. DALE: Objection to the form.

A. You're sort of jumping from one thing to another.

Whether I'm -- you're asking me whether I'm familiar within --

MS. DALE: Let him rephrase.

MR. FOX: Let me rephrase the question.

Q. Do you have an opinion on whether anything in this case is Employers Contributions as defined in the bond documents in this case?

A. No.

Q. How about Revenues as defined in the bond documents in this case?

A. No.

Q. You said you've been deposed -- I think you said about 15 times?

A. Estimated.

Q. How many times do you think you've written expert reports?

A. More than 15. I would say probably over 20.

L. SHER

Q. Do you know if a court has ever excluded your expert testimony, in whole or in part?
A. I don't believe it has.
Q. How did you first learn about this matter?
A. I received, I believe, an email from one of the attorneys at Proskauer.
Q. Do you know when you received that email?
A. It was during the week of June 3rd.
Q. Do you know what you were told they were looking for?
A. Yes. I think what they were looking for was an actuary who could explain the difference between actuarial funding versus Pay as You Go.
Q. In your report, you say that you were engaged to respond to a report by Dr. Andrew Samwick; is that right?
A. Continuing that sentence, I said particularly with respect to the issues that I'm -- that I opined on.
Q. Did counsel tell you what they meant by "respond"?
MS. DALE: Just answer that yes or no.
A. No.

L. SHER

Q. You said you wanted in particular the actuarial valuation reports.

Why was that?

A. Well, I'm an actuarial expert, and I knew that this case has something to do with the funding of the -- of the ERS, so I thought it would be appropriate for me to, for no other reason, to get some background to see what the actuarial reports looked like.

Q. Does anything in your report rely on the actuarial reports?

A. I don't think so. I mean, I would have to review it to be sure, but I don't recall there being anything that relates at least directly to them.

Q. Does anything in your report rely on Act Number 106 2017?

A. I don't think so.

Q. Does anything in your report rely on the expert report of Dr. Sabry?

A. No.

Q. Did you reach any opinion about the expert report of Dr. Sabry?

A. No.

L. SHER

The fact that's what our standards of practice instruct us to do, using a term that can be interpreted in a variety of different ways like that.

Q. Give me an example of one way you might interpret that term.

A. I think one possibility would be -- in one extreme would be if over a period of time that the plan is not being funded in a reasonable actuarial way, to -- with the -- especially if there's a potential of the fund running out of money. If that's becoming imminent, there aren't protections that would be of concern, I don't know that I would use the term "it's not actuarially sound."

What I would prefer to do is state what the facts are and not use a term that's so potentially misleading.

Q. That description that you just gave of a plan that's not being funded in a reasonable actuarial way with the fund running out of money, do you have an opinion whether that's described the ERS in 2017 before the change to Pay as You Go?

A. I would say certainly at that point in

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time there was a significant danger, absent some intervention, that the plan would run out of money, not being funded in a reasonable actuarial way at that point.

Q. Going back for a moment to Appendix 2 to Exhibit 1, am I correct that you did not look at any statutes other than Act 106 2017?

A. I believe that's true.

Q. So you did not look at any other statutes that governed the ERS before act 106 was passed?

A. I don't recall looking at any others, no.

Q. Have you ever used the term "actuarially sound" or "not actuarially sound" to refer to a pension plan in the condition that we were just talking about, that is --

A. I don't --

Q. Do you understand what I mean?

A. I understand what you mean, and I don't recall using that term.

Q. You also looked at a number of financial statements for ERS, right?

A. Or in part, yes.

Q. Is anything in your report based on your review of those financial statements?

L. SHER

A. I don't believe so.

Q. And I think you've already said this, but you did not look at any of the documents that govern the ERS bonds?

A. That's correct.

Q. Have you looked at any deposition testimony in this case?

A. I looked at Dr. Samwick's deposition testimony.

Q. And aside from Dr. Samwick's deposition testimony, have you looked at any additional documents since you served this report?

A. Not that I recall.

Q. You said that you wrote this report, right?

A. Yes.

Q. Did you provide a draft?

A. Yes.

Q. Who did you provide a draft to?

A. Counsel.

Q. Did you receive comments?

A. Yes.

Q. Did they ask you to add anything?

MS. DALE: You can answer that yes or

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on the next page?
A. Yes.
Q. Are paragraphs 8 and 9 the full summary of opinions in this case?
A. Yes. Summary of my opinions. In some cases I elaborate as you get into the report, but it's intended to be a summary of my opinions.
Q. Of course.
Do you agree with me that nothing in paragraph 8 or paragraph 9 discuss Puerto Rico specifically?
A. Yes, I agree.
Q. Do you agree with me that nothing in paragraph 8 or 9 discuss ERS specifically?
A. I agree, yes.
Q. Am I right that paragraphs 8 and 9 describe differences in general between a funded system and a Pay as You Go system?
A. Yes.
Q. Am I right that they describe those differences in terms of a plan in which benefits are still being accrued?
A. I would say as a general matter, yes.
Q. When you say as a general matter, is

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this is just a matter of convenience for some reason to put it in the plan rather than to pay people directly. The money's going right out, I would say that's Pay as You Go.

Q. And you would say that's not a contribution?

A. That's correct.

MR. FOX: We've been going for about an hour. Let's take a break.

MS. DALE: Sure.

THE VIDEOGRAPHER: 3:07. We are off the video record.

(Whereupon, there was a pause in the proceeding.)

THE VIDEOGRAPHER: 3:16. We are on the video record.

Q. Dr. Sher, before we took a break, we were talking about paragraphs 8 and 9 in your report.

Moving beyond paragraphs 8 and 9, do you agree with me that paragraph 20 of your report is the only part that talks about Puerto Rico specifically?

A. I believe that in addition to that paragraph, paragraph 24 is responding to Dr.

Samwick's quoted language in paragraph 21, the third sentence where he refers to Pay-Go.

Q. Your response in paragraph 24 says that the cost of paying benefits under a funded defined benefit system can be materially lower in the long term.

And then it goes on. Do you see that?

A. I'm sorry. Which paragraph are we looking at now?

Q. 24.

MS. DALE: In the second line.

A. Yes, I do see that.

Q. Does anything in paragraph 24 say whether --

MR. FOX: Let me rephrase that.

Q. Does anything in paragraph 24 say anything about Puerto Rico specifically?

A. Not directly.

Q. Does it do so indirectly?

A. I would say that it does in the sense that -- the third sentence of the quoted language in paragraph 21. There's an implication that I took from that sentence that if the system, the ERS system, had always been Pay as You Go that

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everything would have been the same. It wouldn't have mattered.

All it is is timing. The costs of the benefits would have been the same. That's why I responded to it the way I did. It sounds like a general response, but it also is directly in response to what he's saying there and the implication that I took from that, or the inference, I guess.

Q. Do you say in paragraph 24 whether the change to Pay-Go improved or altered benefit payments or the cost of paying benefits in Puerto Rico?

THE WITNESS: Can you read that back, please.

(Whereupon, the requested portion of the record was read.)

A. No.

Q. In paragraph 24, you say that the cost of paying benefits under a funded system can be lower than under a Pay as You Go system; is that right?

A. Yes, lower in the long term, yes.

Q. Can you think of a circumstance in which the cost under Pay as You Go --

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But assuming that everybody's receiving the same benefits, there wouldn't be an effect on the actual benefits, assuming they're all paid for, that all those payments are made.

So in terms of the cost -- I mean, right now the costs that are being incurred are the Pay as You Go costs. It would be hypothetical at this point to say what would have the costs been if this plan continued as opposed to what the Pay as You Go costs are going to be. Is that what you're getting at?

Q. Yes. As an actuary, you estimate what future costs will be, right?

A. You estimate the value of future benefits and then you do some type of allocation to time periods in order to finance them.

Q. So my question to you is: As an actuary, do you have any reason to think that the switch to the Pay-Go system saved money itself? Saved money on benefit payments?

MS. DALE: Objection to the form.

A. I don't know.

Q. Can you think of a way in which it would have had that effect?

L. SHER

A. If the benefits are cut back, it certainly would.

Q. Aside from a change to the benefits, can you think of any other way?

A. Again, when you're saying save money, as compared to what? What am I comparing the save money to? They ran out of money. There's -- I can no longer compare it to something.

If they had funded the plan on a full actuarial basis, then we're in a hypothetical. They didn't do that. When you say save, it has to be relative to something.

Q. Suppose that instead of converting to the Pay-Go system, they had increased employer contributions to ERS sufficient to fund current benefits. That's what I want you to compare it to.

A. Sufficient to fund it now or have they done that in the past?

Q. Now. In 2017.

A. And how would one have determined that funding? To be putting in how much? All the money right up that you need to fund all the future benefits with no amortization? Or to fund a part of it now and some in the future?

L. SHER

Q. The amount they would have needed in order to pay ERS benefits that year.

A. That's Pay as You Go.

Q. So it would be the same amount of money?

A. I don't know. If it's not invested and all they're doing is putting the money in and taking it right back out, I can't see how it would be any different.

Q. Does anything in paragraph 20 -- going back to paragraph 20 -- refer to the Pay-Go fee?

A. I didn't use that term. I talked about the Pay-Go system. But I think my intention was making the payments to cover the actual cost of pension plan payments as they come due, that the intention of the Pay-Go fee was to provide for that.

Q. Who do you understand the Pay-Go fee to be paid to?

A. The Commonwealth General Fund.

Q. Have you heard of something called the accrued pension payment account?

A. Yes.

Q. What do you understand that to be?

A. I understand that to be a mechanism where money that is coming in from the Pay-Go fees would

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temporarily reside with the idea of, you know, then somebody writing out checks or sending them in some electronic way to participants and would come right back out. It might have received some money, seed money, up front from sort of residual assets that the pension systems had. Some may be illiquid assets that had to be liquidated, but that would be just a one-time thing.

But over the long term, the way I viewed that was that it was a convenience. It wasn't intended to be a fund that was going to amass more than the current benefits would require. If that much. Assuming everybody actually paid it.

Q. You agree there's a risk that not all those fees would be paid, right?

A. I think there is a risk, and my understanding is if that were to happen, the Commonwealth would be responsible for the difference.

Q. When you say the Commonwealth would be responsible for the difference, do you mean they would pay the Pay-Go fees or that they would pay the pensions?

L. SHER

the language at this point as to exactly what it says, but I know that the outcome was that the employees would -- if those Pay-Go fees were not paid to some degree, that employees nevertheless -- retirees would receive their full benefits.

Q. Do you agree that Pay-Go fees are a source of funding for the pension benefits that are owed to retirees?

A. I would say they're not funding in the normal sense. There's money that is being transferred over to pay out the benefits. I wouldn't necessarily call it funding, but again, I view funding as -- you know, I'm funding for my kids' education. I'm not doing that in the first year that he's going to college. That would be taking money out of my current income. You know, funding has an advance connotation to me more than just paying it in and out.

Q. Let me rephrase the question.

Are Pay-Go fees a source of money to pay the pension benefits owed to retirees?

A. Yeah. Yes.

Q. We were talking about the accrued pension payment account. Do you know if that is part of the

General Commonwealth Fund?
A. I think it is. I saw language to the extent that it's segregated. I don't know what the point of segregating it really is, because it's going to have -- I think, if I understand it right, it's going to have little or no balance over time, because money is coming in and out.
I mean, it's something that -- it sounds like it's something that may be more than what it's really doing. It's not really setting aside a lot of money to pay things in the future where there might be some fear that it could be raided for other purposes. I don't know how you raid something when money's coming in and out.
Q. But you did see that it's supposed to be segregated?
A. Whether the word "segregated," it was something like that.
Q. Did you see a reference to it being a trust?
A. I don't recall that.
Q. Could you turn to paragraph 13 of your report.
A. (Witness complies.)

L. SHER

MR. FOX: For the record, that's Exhibit 1.

Q. Is it fair to say that this paragraph describes as unfunded accrued actuarial liability can occur if actuarial assumptions are not realized?

A. Well, that's one of the potential causes that's mentioned here.

Q. You also mention that investment returns can be different than expected?

A. Yes, and that would be one of the actuarial assumptions not being realized.

Q. What else do you mention here other than actuarial assumptions not being realized?

A. If contributions are not made at a certain level, you could very well have an increase in an unfunded liability.

Q. Can you point me to where that is in paragraph 13.

A. The very last sentence.

Q. Do you have an opinion about whether the cause --

MR. FOX: Let me back up.

Q. Do you agree that ERS by the start of 2017 had very substantial unfunded accrued actuarial

liabilities?

A. I would agree with that.

Q. Do you have an opinion on the cause of those unfunded accrued actuarial liabilities?

A. I have a general opinion that at least a portion of it was because contributions in at least some prior years were not made at adequate levels.

Q. Do you know if the unfunded accrued actuarial liabilities were primarily the result of that or of actuarial assumptions not being realized?

A. I didn't get into that kind of analysis.

Q. But you agree that sufficient contributions were a part of it?

A. From what I saw, looking at the actuarial valuation reports, that appears to be the case.

Q. Can you turn to paragraph 16.

A. (Witness complies.)

Q. You write in the first sentence: The bottom line, however, is that no matter how projected benefits are assigned to years of service, for a cost method to be considered, quote, actuarial, end quote, it must assign costs to periods of employment.

Do you see that?

L. SHER

A. Yes.
Q. What is the significance to you of whether a cost method is actuarial or not?
A. Well, if I as an actuary are going to make a recommendation, which the actuaries, actually, I think, were doing here, albeit indirectly, I would want the user to know I followed actuarial principles and practices.
Q. You're not suggesting here that whether a cost method is actuarial has some legal significance, are you?
A. No.
Q. You're not suggesting it has some broader economic significance?
A. Well, I would say it has -- it does have significance for accounting purposes, for financial statement purposes. You know, employers, if they're going to comply with accounting standards, certify, get a clean audit, they're going to have to comply with accounting standards, and accounting standards are actually are what all those actuarial reports were primarily focusing on.
They weren't focusing so much on funding, not directly, because funding was

L. SHER

determined, predetermined by law.

Q. When you talk about accounting standards, you're talking about GASB 67 primarily?

A. That's the current standard.

Q. But to go back to my question, you're not suggesting that whether a cost method is actuarial has some economic significance, are you?

A. Certainly not directly. I think using an appropriate actuarial cost method is, I think, advisable as -- you know, if it could be followed, I think it is much more likely that the benefits ultimately can be paid and that there won't be any major disruption to the system.

That's really the purpose, to come up with a rational series of contributions that are fairly predictable, fairly stable, and you don't have to rely on future stockholders or future taxpayers. That's the purpose of funding on an actuarial basis.

Q. That description that you just gave of a rational series of contributions that are fairly predictable, fairly stable, and you don't have to rely on future stockholders and future taxpayers, do you know if that describes the contributions to ERS

before 2017?

A. They were not funding on an actuarial basis. That was -- you know, I can tell that much from reading the actuarial reports and the warnings that were provided in the later years.

So yes, any system in Puerto Rico is by no means alone. This is going on in New Jersey and all over, particularly in the public sector, where actuaries make recommendations and legislators don't follow them, and a lot of them have gotten themselves into financial difficulties.

Q. To be clear, you agree that Puerto Rico was not funding ERS on an actuarial basis for 2017; is that right?

A. I would say that's true.

Q. You say -- going on in paragraph 16 -- that there was an exception with respect to the amortization of any unfunded actuarial liability.

Do you see that?

A. Yes.

Q. Do you know whether ERS as of 2017 had any --

MR. FOX: Let me rephrase.

L. SHER

Q. Do you know whether ERS as of 2017 had new benefits accruing under the traditional defined benefit pension plans?

A. I don't believe -- I think all benefits had been frozen at that point.

Q. Is it fair to say the only contributions being made before 2017, but leading up to 2017, were amortization of unfunded accrued actuarial liabilities?

A. Once benefits were frozen, the only requirement, the only need you had was to build up the assets from where they were to what you're going to need to pay all the future benefits that had been accrued.

So that difference has got to get into the plan in some way at some time. Before the fund runs out of money, preferably.

Q. And so I think that's in agreement with my question, which is that the only contributions being made were the amortization of unfunded accrued actuarial liabilities.

Do you agree?

A. Well, I agree in the sense that that's a practical effect of it. I think the contributions

were statutorily required. I don't think the legislature thought about that those contributions were being earmarked to do any one thing or another.

You know, in actuality, yes, the only thing they're doing is helping to pay off the unfunded liability.

Q. What I'm trying to get at here, in the first paragraph you state a rule of what's required for cost methods to be actuarial, right?

A. Yes. I state -- where are we?

Q. 16. Sorry. Let me rephrase that question.

In the first sentence you state a rule for what is required for cost methods to be actuarial?

A. And then I indicate what the only exception is.

Q. Right. I think we agree that the exception applied to ERS leading up to 2017?

A. Yes. Once the plan was frozen, that's true.

Q. In paragraph 18, you describe a Pay as You Go approach as a nonactuarial approach.

Do you see that? It's on the third

line.

A. Yes.

Q. What is the significance to you of a Pay as You Go approach being nonactuarial?

A. Well, I would say that there's no prefunding of benefits as they were being earned. There's no fund. There's no contributions. There's only once somebody retires, you pay them the benefits. That's not an actuarial approach.

An actuarial method would -- with the exception of the amortization I mentioned -- call for funding all of the benefits that are accruing for any individual during their working career before they retire.

Q. But you agree that by 2017, ERS was covered by that exception that you mentioned, right?

A. I mean, I agree that by 2017, the funding, any of the funding there was being made to the plan, was being made to -- for the purpose of amortizing the unfunded liability. It's not a Pay-Go at that point. All right? It's funding.

Q. But you agree that the employer contributions -- I think you said earlier -- being made were nonactuarial as well before 2017? Right?

L. SHER

A. They were not satisfying an actuarial approach, because they were not, in some systemic way, funding all of the benefits as they were being earned.

Q. And that remained true --

MR. FOX: Withdraw that.

Q. If you look at paragraph 19. I'm not going to read this to you, but do you agree this is discussing a Pay as You Go in general and not the Pay-Go system in Puerto Rico specifically?

A. Yes. It is not referring to Puerto Rico.

Q. Do you see on page 7 there's a sentence that begins "by contrast"?

MS. DALE: Second line.

A. Yes.

Q. And that, I take it, is not describing ERS, but is describing a funded system in general?

A. Well, I would say yes with the caveat that it's better to have some assets accumulated than have no assets accumulated.

The last sentence says: The more assets that are accumulated before employees retire, the less reliance there will be on the ability and willingness of future funding sources

to come up with potentially rising funding requirements.

So yes, they were not funding on an actuarial basis, but they were -- apparently for a very long time, maybe since the 1950s -- funding at something less than -- or maybe they were funding perfectly for a while. I don't know. I don't know when they diverted from that. I don't have that information.

But at least in recent years, they were not funding on what I would call an actuarial method.

Q. By 2017, do you agree that they were on the verge of running out of money?

MS. DALE: Now we're talking about ERS, correct?

MR. FOX: Correct.

A. I believe that's true.

Q. If you turn to paragraph 21. Now we start to get into your disagreement with Dr. Samwick; is that right?

A. Yes.

Q. Do paragraphs 21 to 24 fully describe your disagreements with Dr. Samwick's report?

A. I think they describe my disagreements with his report to the degree that it deals with the issues that I was asked to opine on.

Q. Are there any opinions about Dr. Samwick's report that you intend to give in this matter that are not in paragraphs 21 to 24?

A. Not as I sit here now. I don't believe so.

Q. In paragraph 23, the first sentence, you write: I disagree with the first sentence, because under a Pay as You Go approach, there are no contributions and no funding.

Do you see that?

A. Yes.

Q. And I think we discussed earlier that you used the word "funding" to refer to funds that are invested; is that right?

A. Well, I'm referring to a fund where normally the money -- unless it's going right in and out, normally you would expect the monies would be invested, yes.

Q. So why do you say there's no funding under a Pay as You Go system?

A. Because there are -- the monies are

either going directly to participants or they're going -- flitting through some account that probably would have no opportunity to invest or very limited opportunity to invest.

In other words, the purpose of having any kind of account like that is really a matter of convenience so one can write out the checks. It's basically an administrative function, not an investment function.

Q. When you say no contributions, I think it's for a similar reason. Because the money is not being contributed to be invested for the future; is that right?

A. Yeah. A contribution, to me, has to be something that is intended to be invested and to be applied at some future date to make payments sometime in the future, not to be making them currently.

Q. Paragraph 23 is a description of a Pay as You Go system in general?

A. I would say so, yes.

Q. Nothing in there about Pay-Go specifically?

A. Not in there specifically, no.

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Q. Paragraph 24 we talked about a little bit already, right?
A. I believe we did.
Q. And I believe you agreed that this a description of a funded system in general and not ERS specifically, right?
A. Yes.
Q. Do you recall from your review of Dr. Samwick's report if Dr. Samwick also reached conclusions about ERS specifically and Pay-Go specifically?
A. I recall there being some confusion at points where -- sometimes either in the same paragraph or maybe even sentence where it wasn't clear. He capitalized the word "system," for example. I recall this from his deposition.
Other than that, I'm not sure how to answer your question. I think he bounced back and forth, perhaps.
Q. You did see some discussion of Pay-Go and ERS specifically?
A. Yes.
Q. Fair to say there's no criticism of that discussion in your report?

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A. I -- I don't -- I'm not sure. I mean, to the extent it's beyond what I've indicated here, there is no discussion of it. But I'm not sure exactly what you're referring to in his report.

Q. But you agree that what you have in paragraphs 21 to 24 is about Pay as You Go in general and funded systems in general?

MS. DALE: Objection. Misstates his testimony.

A. Well, there's nothing directly in my 21 to 24 that focuses on Pay-Go. I view Pay-Go as a Pay as You Go system. So to the extent what I'm saying deals with Pay as You Go, it would necessarily deal with Pay-Go. But I stated these as general propositions.

Q. In terms of ERS, there's nothing in 21 to 24 that addresses ERS specifically?

A. I don't believe so, no.

Q. Do you agree that ERS by 2017 did not always follow sound actuarial practices?

MS. DALE: Objection to the form.

A. Well, we're back to the "sound" word.

MR. FOX: Let me rephrase.

Q. What term would you use to describe a

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pension plan that follows actuarial requirements?
A. I would say that the plan is being funded in accordance with actuarial standards of practice.
Q. Do you agree that by 2017, ERS was not being funded in accordance with actuarial standards of practice?
A. I would agree with that.
Q. Is it within your expertise as an actuary to put a dollar value on future uncertain liabilities?
A. Well, certainly an actuary is called upon to make calculations of financial promises like pensions or insurance, you know, financial instruments like those, by making assumptions regarding the future, all kinds of assumptions.
The actuary generally would have the expertise to do the research or find other ways to come up with assumptions that he or she feels are reasonable. They're not predictions. They're assumptions.
Q. Would you describe that process that you just described as valuation?
A. Well, a valuation certainly does that type of thing. It takes employee data for the

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participants who are covered under the plan, whether they be active or retired, and they take into account the benefit provisions of the plan or plans and they make assumptions as to what might happen in the future in terms of demographics, the individuals, how long are they going to work, how long are they going to live, what are they going to get paid.

And then, of course, there's the discounting approach, coming up with present values. And then it's a distribution of that over time, the funding method.

Q. Does the purpose of the valuation affect what sort of assumptions are reasonable?

A. It can.

Q. Do you agree that when --

MR. FOX: Let me back up.

Q. Is one of the things an actuary does discounting the future liabilities of a pension plan?

A. Well, it's one of the things. It's discounting the projected benefits along with discounting for outlet contingencies that might arise, both before benefits start and while they're

being paid, discounting the value -- you know, the amounts of those benefits potentially payable to a current year or date. That's all part of the process.

Q. When an actuary does that, do they assume that the pension benefits will be paid as required?

A. They generally do. Certainly the starting point is the benefits that current exist, you know, in some type of a legal document, plan document, typically.

To the extent that there's any need to reflect different plan provisions because there are changes that are forecasted to occur in the future or that hypothetically might occur in the future, you know, the actuary might provide various scenarios.

But normally it would be, you know, reflect as a starting point the benefits that are being promised.

Q. Would the actuary consider the possibility that the plan would default on the payment of its benefits?

A. I would say normally no, that most actuarial work is done on the presumption that the

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-- that the benefits are going to stay the same and that the funding source is going to be able to pay those benefits, unless the actuary -- unless something actually happens to change that or the actuary is instructed to make some other kind of calculation.

Q. Do actuaries also value assets?

A. In a limited way. I would say most of the time these days, actuaries just take the market value of assets, assuming they're reported to them by a trustee and they're all marketable securities and there aren't any special kind of valuations that need to be done on illiquid assets.

Sometimes actuaries introduce an averaging or a smoothing technique in an attempt to try to stabilize the resulting financial values and costs.

If the assets tend to fluctuate widely, there's one school of thought that a better approach is to smooth those ups and downs. But I would say the trend is towards reflecting the current or market value of the assets.

Q. You referred to special kinds of valuations that need to be done on illiquid assets.

assets?

A. They certainly -- when they're valuing the value of a business, when they're valuing -- when an investment banker is trying to put a value on a business, they would -- one of the methods is to discount future projected cash flows coming from the business.

In the pension scheme, generally you have to choose a rate or rates to discount the value of the projected benefits to get a liability, or what you're calling a liability.

But the assets themselves are valued at market. That's what's done for accounting purposes as well.

Q. If you know, when an investment banker is using the process that you described of discounting future projected cash flows, does the discount rate they use reflect the risk of those cash flows?

A. Well, I'm not an investment banker, and it's been a while since I've worked directly with one. I would think it's very possible that they do, but I don't have any direct knowledge or recollection at this point.

Q. Going back a little bit, I think you said

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earlier that if an actuary faces uncertain possibilities, one thing they might do is assess various scenarios and describe the outcome under those various scenarios; is that right?

A. They could if they're asked to do that. If whoever's paying their fees wants them to do some type of a risk assessment as to what would happen in the future under various different scenarios, they could be economic scenarios. They could be workforce scenarios. Actuaries certainly do that.

Q. What is the purpose of providing information about different scenarios?

MS. DALE: Objection to the form.

A. When I've been asked to do that in the past, it's usually because the -- whoever's asking for that -- usually it's a financial person, a CFO or a treasurer, for example -- wants to understand the range of reasonable outcomes that might occur over a period of time. Usually it's over a five- to ten-year period, in my experience.

They would want to do some forecasting perhaps to fit in with other forecasting that they're doing for other parts of their business, and they would ask the actuary to do projections

of contribution requirements, of accounting costs, benefit payouts.

That's done quite often, I would say.

Q. Is there an actuarial standard that governs where one pension plan ends and another pension plan begins?

A. I'm not sure -- can you be more specific as to what you mean, when one pension plan ends and one pension plan begins?

Q. If you're looking at a set of pension benefits as an actuary, how do you know if you have one pension plan or two pension plans?

A. Well, I think you get documents that embody the pension benefits that you are about to make calculations on. Usually it's a plan document. Sometimes there may be more than one where there's some kind of coordination of benefits, say, between two plans where one plan may be determining a benefit and the benefit from the other plan is being offset from the first plan's benefit.

In that case, you would have to understand what that second plan is providing in addition to what the first plan is providing.

Q. Have you ever advised a pension plan on

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a different version of the same pension plan?
A. Let me make sure I understand. So it's the same terms of the plan? The same funding source? Just covering different people?
Q. So it's the same benefits being paid to the same people.
A. Okay.
Q. From the same sponsors.
A. Why would there be more than one plan?
Q. That's my question to you. Is that the same pension plan or a different pension plan?
A. I guess I can't think of a scenario where I've run into something like that. I wouldn't know why it's being set up that way.
Q. Suppose that there was some change made in the contribution formula.
A. Employee contribution formula?
Q. The employer contribution formula.
A. All right. Sounds like you're getting very specific. Is this totally hypothetical or are you trying to relate this to something in this case?
Q. I'm asking you a hypothetical.
If you have a pension plan and then a change is made to the contribution formula that

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employers pay but the benefits are the same, they're paid to the same people, and the employers who fund the plan are the same employers, my question to you is does that sound like the same pension plan or a different pension plan?

A. That sounds like a legal -- you're into a legal question, you know, what does it mean to be in the same pension plan? Does it mean -- does not have anything to do with what might happen if the assets were to run down or -- I just can't really think of a scenario in the real world that I've run into that fits what, at least I understand, you're describing.

Q. So you can't think of an actuarial standard that would distinguish under those circumstances between the -- that would suggest that, as an actuarial matter, there's a separate plan?

MS. DALE: Objection to the form of the question.

A. I don't -- I don't think there's an actuarial standard that deals with something along the lines as you're describing, at least as I understand it.

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Q. Anything other than the change in source that you can think of?

A. I can see a retiree having some at least perception of once the source is different, you know, whether that would -- you know, a particular retiree would feel more or less comfortable with one source versus another.

Q. Are you offering any opinion about whether the Pay-Go fees are a substitute for employer contributions?

A. I don't believe so.

Q. Any opinion about whether the Pay-Go fees are proceeds of employer contributions?

A. Whether they are proceeds of employer contributions?

Q. Yes.

A. Well, I don't think -- I wouldn't characterize them as contributions, so I don't know how they would be proceeds of contributions.

Q. You're not offering any opinion about whether Pay-Go fee are the economic equivalent of employer contributions?

A. No.

Q. We agreed you're not an expert economist?

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A. Yes.

MS. DALE: We have agreed that.

Q. Footnote 9 -- if you turn back to Exhibit 1, do you see footnote 9 on page 7 of your report?

A. Yes.

Q. You list there five paragraphs from Dr. Samwick's report?

A. Yes.

Q. Is your disagreement with Dr. Samwick in those five paragraphs fully expressed in paragraphs 21 through 24?

A. I would say so. I would say that the -- his language was similar to what I've quoted here, which was from his summary. I think the other sections are actually in the body of his report, the other paragraphs. I think they're analogous -- my comments and issue here would be analogous of the other paragraphs.

MR. FOX: Thank you. That's all I have?

MR. WEDOFF: Nothing from the retirement committee.

MS. DALE: We don't have anything.

THE VIDEOGRAPHER: 4:45 p.m. We are